

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

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| PETITION OF B & H GAS COMPANY |) | |
| FOR AUTHORITY TO ADJUST RATES |) | CASE NO. |
| IN ACCORDANCE WITH THE PURCHASED |) | 8135-A |
| GAS ADJUSTMENT PROCEDURE |) | |

I N T E R I M
O R D E R

On June 17, 1981, the Commission issued its Order in Case No. 8135, approving a purchased gas adjustment ("PGA") clause for B & H Gas Company ("B & H") and providing under certain conditions for the further adjustment of rates when the wholesale cost of gas is increased or decreased or re-funds are received.

On August 13, 1981, B & H requested authority to pass through to its customers an increase from one of its suppliers, S. J. Bradley and Son ("Bradley"). The effective date of the increase from Bradley was September 1, 1981. B & H failed to provide information on its financial condition and information required to convert Bradley's increase to an Mcf basis, all of which is required by the Commission's Order establishing the PGA.

On September 24, 1981, B & H filed a balance sheet and income statement and the dollar amounts paid its two suppliers, Bradley and Gypsy Hughes' Wells ("Hughes"). However, it provided no information on the number of Mcfs purchased or sold.

On November 2, 1981, the Commission ordered B & H to furnish the number of Mcfs purchased and sold, amount of increase in revenue and the new or proposed rates.

On November 13, 1981, in response to the Commission's Order, B & H filed a schedule showing the number of Mcfs purchased or sold. B & H also furnished a calculation showing a requested increase in revenue of \$78,179,176 and an increase in rates of \$2.53 per Mcf.

The Commission's analysis of the information contained in the filings showed that Bradley had proposed to sell gas to B & H at \$.80 per Mcf, which represented an increase of \$.33 per Mcf. The analysis further disclosed that the primary reason for B & H's request for an increase of \$2.53 per Mcf was to cover a charge of \$3.23 per Mcf by Stanville Transmission Company ("STC"). In the calculation of the increase per Mcf, B & H indicated STC was a successor to Bradley.

The Commission has authority under KRS 278.040(2) to regulate the price paid for intrastate transmission of natural gas for resale. A review of the Commission's records revealed that it had not received a request for a certificate of convenience and necessity from STC for intrastate transmission of natural gas.

In December 1981 and January 1982, customers of B & H notified the Commission's Secretary that B & H was charging rates significantly higher than those approved by the Commission. A review of copies of bills filed by B & H's customers disclosed that B & H in fact was charging the rates requested in its November 13 filing.

Based on the above information, on December 7, 1981, the Commission ordered B & H to charge the rates authorized in Case No. 6690, and scheduled a hearing to determine the appropriateness of the requested PGA rate and to consider the transactions which resulted in B & H changing its requested increase from \$.33 to \$2.53 per Mcf. A hearing was held on December 21, 1981, at the Commission's offices in Frankfort. The case has been submitted for final determination.

The witnesses appearing at the hearing were: Avery Harmon, President of B & H; John Bradley, a 50 percent partner in Bradley; Danny Preston, President of Johnson County Gas Company, Inc., ("Johnson") and a one-third partner in STC; Robert L. Abrams, managing partner in the certified public accounting firm of Helton, Butler and Wells, and a one-third partner in STC; and Phillip Woods, President and owner of the stock of Stanville Gas, Inc., ("SG") and a one-third partner in STC.

Because of the importance attached to this proceeding, the Commission has included the following thorough review of testimony received at the December 21 hearing:

Mr. Harmon testified that B & H charged the \$.33 per Mcf increase from Bradley for 2 months beginning October 1, 1981, and that the increase from STC of \$2.52 per Mcf was billed customers on December 1, 1981. He further testified that B & H had not received an Order from this Commission authorizing the rates charged in October, November and December; STC had contracted with Bradley in October to purchase all of its production at \$.80 per Mcf; he had applied for approximately 20 Mcfs per hour of

additional gas supply from Columbia Gas for existing and anticipated new customers; approximately 25 new customers could be hooked up at the present time; the quantity of gas offered by STC is approximately the same as the quantity previously received from Bradley; the 20 Mcfs were needed to replace an additional source of gas, Hughes; in cold weather the quantity from Hughes represented about 20 to 25 percent of B & H's total gas requirements; he was unsure of the total requirements during cold weather, but approximated them at 350 to 400 Mcfs in a 24-hour period; the reason for applying for 350 to 400 Mcfs per day from Columbia was to replace the gas from the alternate source and provide for future growth; the number of Mcfs required per day was supplied by B & H's CPA, Mr. Abrams; the application to Columbia was not complete and for this reason he knew nothing about the rates Columbia would charge; B & H had adhered to the Commission's Order of December 7, 1981, only to the extent that it had not collected the unauthorized rates from customers who based their payment on authorized rates but had accepted them from customers who paid the full amount of the billing rendered on December 1; no customer had been terminated at this point; B & H had maintained the lines from the wellhead to its distribution system until the summer of 1981; B & H had not repaired a line at the river crossing at Ivel because it had no customers on the other side and it was financially unable to do so; he did not consider the lines from the wellhead to the distribution system as B & H's plant; B & H had maintained these lines in order to

get gas; B & H entered into a contract in November with STC to take all the gas STC produced; B & H had contacted every gas producing company in the area in the last year and none would supply it gas except Kentucky West Virginia with assistance from the Commission; B & H is required by its contract with STC to take whatever gas STC produces and that B & H has no recourse against STC for non-performance; STC can discontinue service to B & H for non-performance; B & H had six different delivery points and that his understanding was that the term "point" in the contract referred to these six delivery points; these delivery points range from 50 to 500 feet from the wellhead; B & H had owned both the wells and the distribution company at one time, and that this ownership possibly included the sections of line from the wellhead to the delivery point; he had entered into an agreement to sell the B & H distribution system to SG; he was aware Commission approval of the sale was required; no application for approval of the sale had been made to the Commission; he had entered into a contract that required installation of six purchase meters but had no knowledge of the cost of these meters; and the first bill rendered to customers on December 1 for the STC flow-through was for November usage.

Mr. Bradley, a 50 percent partner in Bradley, testified that he and his father were engaged in producing oil and gas from properties in and around Stanville; Bradley had sales contracts in the past with B & H; Bradley currently has a contract to sell natural gas produced from its wells to STC; the agreement with

B & H was made in 1975 when Bradley sold B & H to Avery Lee Harmon and Kenny Osborne and the price of gas under that agreement was \$.47 per Mcf; the price of the gas was not in the written agreement but was a verbal agreement; the wells and distribution system were one business until October 30, 1975; the production was not sold outside the distribution system; the 1975 agreement included the continuation of Bradley's supplying all production to the distribution system; Bradley did not advise B & H that the production from its wells had been purchased by STC; Bradley had absorbed all line losses; Bradley started charging B & H \$.80 per Mcf in September 1981; Bradley's wells have not been certified as stripper wells; he was not aware of the procedure required to obtain stripper well certification; Bradley did not own the property the wells are located on but held leases on the wells for as long as they produced; prior to the sale of the distribution system the lines from the wells were owned by Bradley but after the sale all Bradley had left were the leases on the wells; Avery Lee Harmon and Kenny Osborne bought the lines, regulators and meters in 1975; no other entity owned any part of the B & H system including the lines from the wellhead; Bradley had transferred no property to STC; Bradley entered into a contract which requires STC to take delivery of gas at the metering point which is the wellhead; he did not know what new meters would cost; the agreement with STC contemplates that production will be metered and that the lines from the meter to the distribution system would be maintained by STC; STC had put in the river crossing at Ivel; and that Bradley has no agreement,

oral or written, that requires STC to put in meters at the well-head.

Danny Preston, President of Johnson, testified that STC was a partnership; the three general partners were Danny Preston, Phillip Woods and Robert Abrams; each partner had a one-third interest; the facilities owned by STC were the lines from the wellheads to the distribution system; STC had no legal title to the land or the lines on them; STC ownership was by possession; none of the lines claimed extended outside Kentucky; STC did not have a certificate of convenience and necessity ("CCN") from this Commission; he did not know whether an application for a CCN was pending; STC had no managing partner; STC fixed the price of its gas sold to B & H at the minimum stripper well price; he did not know if the wells had been classified as stripper wells; he did not know what contribution, if any, was required by the partnership agreement; his contribution consisted of supplying materials obtained from a newly constructed Johnson system; Johnson either had billed STC for these materials or intended to bill for them; either STC or SG would be obligated to pay for these materials; no independent estimate of the value of materials supplied by Johnson to STC had been obtained; the remainder of his contribution was \$100 (perhaps only \$50) to open a checking account; he did not know if STC's records were maintained under the Uniform System of Accounts prescribed by this Commission; the only customer served by STC is the B & H distribution system; he did not know of any Commission authorization for transfer of B & H to SG;

STC currently buys gas only from Bradley but seeks to obtain additional gas from the Hughes wells; he did not know how much gas was available from Hughes; he had an engineer look at the Hughes wells; the engineer thought the wells were in fair shape but could provide no estimate of their production capability; he did not know what quantity of gas was currently being produced by these wells; he considered himself a full-time employee of Johnson except for advising STC; Phillip Woods was at the Stanville office about every day and would be helped by Avery Harmon; STC's equipment consisted of pipe wrenches, shovels and mattocks; STC would rent heavy equipment by the hour; the owner and operator of the equipment, Avery Harmon, would not necessarily require current payment of rent; he would supply copies of the engineer's reports on both the Bradley and Hughes wells when they were completed; the funds obtained by STC from charging stripper well prices would be put into SG; money had already been advanced by STC to SG; and no obligation exists for STC to SG but one could be established by "the stroke of a pen."

Robert L. Abrams testified concerning his "vision" for Eastern Kentucky; B & H was just "the tip of the iceberg"; B & H is a dilapidated, unsafe company which has had inadequate safety supervision, inadequate rate structures and inadequate sources of supply; B & H had been supervised by this Commission and has reached the point where it is incapable of providing gas on a day-to-day basis to the consumer; many utilities have been reconstructed over the last several years but about 20 still needed to

be rebuilt; the purpose of STC, through the Natural Gas Policy Act, is to operate the gas wells and produce gas on a safe basis; he and Mr. Woods had made no contribution to STC; he viewed their efforts as their contribution; STC intended to make profits of STC available to SG so that it could be rebuilt; these profits would be loaned to SG at the interest rate allowed by the Internal Revenue Service; funds for other systems had been obtained from the federal government at lower rates but this required paying wages under the Davis-Bacon Act and unnecessary supervision that increased construction costs; the engineer for the Johnson rebuilding estimated that it could have been done at one-third to one-half the cost absent federal intervention; the inadequate supervision to which he referred was that of the Commission; he thought a president's role was to provide a safe, sound system that could provide employees, maintenance and an adequate return to shareholders; the president of B & H had tried to do this but had been rebuffed by the Commission which provided no guidance in rate relief, maintenance or safety; he did not know Mr. Harmon's education nor training regarding gas safety, operation, financing or any area relevant to running a company; he had only reviewed past annual reports to the Commission; Mr. Harmon was hired to operate SG on the basis of Mr. Woods' recommendation; SG had \$1,000 in capital paid in by Mr. Woods; he hoped Mr. Woods would engage him to keep the records of SG; he did not know which company had contracted with Heath and Associates for a leak survey; he had provided verbal assurances to a Mr. Turpish that

the survey would be paid for; the only deposits to STC's checking account were \$50 to open the account and a partial payment from B & H; disbursements consisted of \$3,036 to Bradley and \$900 to Mr. Woods; disbursements by SG were \$5,000 to B & H and \$900 to Mr. Woods; SG's only activity had been to provide a salary to its only employee and make payments on its option to buy B & H; no inventory existed for STC; the estimated expenses for the partnership were \$32,000; the calculation of 20 Mcfs per hour was based on the maximum possible usage and that the 20 Mcfs per hour would be bought around the clock; he had not been involved in any negotiating with Columbia Gas; he did not know the maximum usage at the peak hour of the peak month of the year; the request for 20 additional Mcfs from Columbia was "a best guess"; he had access to Mr. Harmon's records; after exploring actual requirements the request to Columbia would be modified if required; STC buys gas from Bradley at \$.80 per Mcf; the price charged B & H is \$3.23 per Mcf; the profit to STC on gas sales to B & H would be \$97,000 per year; the price to the customer would increase from \$1.50 to \$2.00 per Mcf over and above the cost billed in November if the distribution system is rebuilt; the estimated cost of rebuilding was approximately \$500,000; no estimates of the cost of rebuilding had been obtained from contractors; the rates billed in December were \$8.55 for the first 2 Mcfs, \$4.03 for the next 8 Mcfs, \$3.70 for the next 20 Mcfs and \$3.62 for all over 30 Mcfs; and under current Commission Order, the rate billed in January would drop back to \$1.50 per Mcf.

Mr. Woods testified that he had not paid all of the \$1,000 required by SG's Articles of Incorporation; the amount currently in the checking account is \$250; the leak survey will cost approximately \$250; he did not have proof that he was certified to operate a gas distribution system but believed he could produce proof and agreed to supply it later; he had 6 years experience with Platco Corporation in Pennsylvania; he had done everything from rotary drilling to hooking meters for fuel taps; he or STC had paid \$10,000 for option to purchase B & H; and initially it was his opinion that SG was not obligated to purchase gas from STC, but later was uncertain what his obligation would be if SG purchased the assets and liabilities of B & H.

Based on the evidence of record the Commission finds that:

1. Bradley and Hughes are producers of natural gas and B & H is a distributor of natural gas and all are public utilities as defined by KRS 278.010(4)(b).
2. B & H is the only utility certified by this Commission to provide retail gas service to customers in and around Stanville, Floyd County, Kentucky.
3. KRS 278.040(2) gives the Commission exclusive jurisdiction over the rates charged by public utilities.
4. By agreement dated October 14, 1981, B & H granted to SG an option to purchase all of its assets.
5. B & H has not filed an application to sell its gas properties and neither STC nor SG has filed an application to acquire the property of B & H.

6. Sale or transfer by a public utility of its property must be approved by this Commission.

7. Neither STC nor SG has received a certificate of public convenience and necessity to engage in the purchase, transmission, or distribution of natural gas. Further, that each is without present legal basis or authority to purchase, transport, or distribute natural gas for compensation in Kentucky.

8. On the basis of the findings in Paragraph 7, B & H should cease and desist from buying gas from or selling gas to either SG or STC.

9. B & H has charged unauthorized rates for billings rendered in December and should cease and desist from charging unauthorized rates for billings rendered in January 1982 and thereafter.

10. B & H should refund to its customers amounts collected in excess of amounts chargeable under rates approved by the Commission.

11. B & H's request under the PGA to pass through an increase of \$.33 per Mcf from Bradley effective September 1, 1981, should be approved.

12. B & H's request under the PGA to pass through an increase of \$2.5259 per Mcf from STC should be denied.

IT IS THEREFORE ORDERED that B & H shall cease and desist from billing any customers for any amounts paid STC and shall cease and desist from buying gas from or selling gas to either SG or STC so long as the facts found in Paragraph 7 as to each of them continue to exist.

IT IS FURTHER ORDERED that the rates in Appendix A which reflect the increase of \$.33 per Mcf from Bradley, B & H's legal supplier, be and are hereby approved for service rendered on and after September 1, 1981.

IT IS FURTHER ORDERED that B & H shall refund to all customers all amounts collected in excess of the rates contained in Appendix A to this Order.

Done at Frankfort, Kentucky, this 15th day of January, 1982.

PUBLIC SERVICE COMMISSION

Marlin M. Vohs
Chairman

Katherine Badall
Vice Chairman

Sam Carreaga
Commissioner

ATTEST:

Secretary

APPENDIX A

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE
COMMISSION IN CASE NO. 8135-A DATED
JANUARY 15, 1982

The following rates are prescribed for the customers in the area served by B & H Gas Company. All other rates and charges not specifically mentioned herein shall remain the same as those in effect prior to the date of this Order.

RATES: Monthly

| | | |
|-------|----------------|-------------------------|
| First | 2,000 cu. ft. | \$4.1040 (Minimum Bill) |
| Next | 8,000 cu. ft. | 1.8020 per Mcf |
| Next | 20,000 cu. ft. | 1.5520 per Mcf |
| Over | 30,000 cu. ft. | 1.4020 per Mcf |